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SUBJECT: KAZAKHSTAN: SOUTH KOREANS SEEKING INVESTMENTS, BUT GLOBAL
FINANCIAL CRISIS SLOWS DOWN BUSINESS

1. (U) Sensitive but unclassified. Not for public Internet.

2. (SBU) SUMMARY: Poloff met several times in January with South
Korean Embassy First Secretary Lee Jooil and Second Secretary Lee
Moon-bae to discuss economic relations between Kazakhstan and Korea.
They explained that overall bilateral economic relations are robust
and that South Korea continues to pursue investments in Kazakhstan's
mining and energy sectors to enhance its energy security. However,
they admitted that falling commodity prices and the global financial
crisis are negatively affecting Korean business interests in the
country. END SUMMARY.

ENERGY SECURITY IS TOP KOREAN PRIORITY

3. (SBU) During a January meeting with Poloff, South Korean Embassy
First Secretary Lee Jooil said that his government's top priorities
in Kazakhstan are energy security and improving economic ties.
Kazakhstan's formidable energy resources and Korean President Lee
Myung-Bak's decision to make energy security one of his
administration's top priorities have made the Kazakhstani-Korean
relationship more important than ever. As an example, Lee noted
that during Prime Minister Han Seung-soo's May 2008 visit to
Kazakhstan, the Korea National Oil Corporation (KNOC) and
Kazakhstan's national oil and gas company KazMunaiGas (KMG) signed
an agreement for KNOC to purchase a 27 percent stake in Kazakhstan's
Zhambyl oil field. (NOTE: According to press reports, the Zhambyl
field is estimated to hold about 1 billion barrels of crude oil.
END NOTE.) Under the agreement, South Korean companies, including
SK, Samsung, and LG, will be able to extract 270 million barrels
over five years. Lee also reported that South Korea has established
the Korean Consortium for Caspian Oil Projects, in which SK,
Samsung, and LG are the largest and companies. (COMMENT: The
Korean Consortium for Caspian Oil Projects appears to be a
combination of a government-driven project to meet Korea's energy
needs and a cost-sharing vehicle to divide up the high expenses of
oil extraction in Kazakhstan among several companies. END COMMENT.)

KOREA REMAINS A MAJOR SOURCE OF INVESTMENT

14. (U) Lee Jooil noted that Kazakhstan and South Korea have had a robust economic relationship since Kazakhstan's independence. For 1993-2006, Korea ranked seventh in terms of cumulative foreign direct investment (FDI) in Kazakhstan, immediately behind Switzerland and in front of China, Canada, Russia, Japan, and Turkey. In 2007, Korean companies invested \$232 million in Kazakhstan, ranking the country twelfth in terms of FDI for the year. Lee expects Korea to continue to be a significant foreign investor in Kazakhstan, although he noted that the global financial crisis is seriously affecting Korea's global FDI flows.

KOREAN COMPANIES ACTIVE IN ENERGY AND MINING DEALS

15. (SBU) The strong bilateral economic relationship is also evident in the number of companies and the size of their activities in Kazakhstan. Since Kazakhstan declared independence, Korean and Kazakhstani companies have established over 300 joint ventures. In one of the largest deals, Samsung announced a \$4.7 billion investment in May 2008 to build a coal-powered electricity-generating plant near Lake Balkhash. (NOTE: Samsung's large-scale involvement in Kazakhstan is not a new development. In 1995, Samsung acquired 75 percent of the shares of Kazakhmys, one of Kazakhstan's largest copper-mining companies. However, by 2005, Samsung had divested itself from its entire stake. At the time of its IPO on the London Stock Exchange, Kazakhmys's largest shareholder was Vladimir Kim, an ethnic Korean citizen of Kazakhstan, who held 46.52 percent of the company's stock. Lee Jooil told Poloff that the Kazakhstani government pressured Samsung to withdraw from Kazakhmys because of its preference for domestic ownership of the company. END NOTE.) Among other recent significant economic deals, in March 2008, the South Korean Electric Power Corporation (KEPCO) signed a memorandum of understanding for a

ASTANA 00000169 002 OF 003

\$500 investment to build a thermal power plant in Astana and increase an existing plant's capacity from 360 to 600 megawatts. Also in March 2008, Daewoo International and South Kazakhstan oblast authorities announced plans to begin construction of a power station in South Kazakhstan in the spring of 2009. In May 2008, the Korea Resources Corporation (KOPEC) and Astana Finance concluded a memorandum of understanding to jointly participate in mining projects dealing with the exploration, extraction, and production of copper, zinc, tungsten, molybdenum, nickel, and rutile in Kazakhstan. Also in May 2008, Korea Hydro and Nuclear Power agreed to buy 3,410 tons of uranium through 2017, amounting to 11 percent of South Korea's annual uranium consumption.

CLASH OF TITANS: KOREANS FACE OFF AGAINST THE CHINESE

16. (SBU) Korean Embassy official Lee Jooil explained to Poloff that Chinese companies are the primary competitors for South Korean firms in Kazakhstan. Lee said that despite the lower operating costs of Chinese companies, Korean businesses continue to win tenders by emphasizing their comparative advantages, such as the high-quality of their goods, advanced technology and know-how, and openness to technology transfers.

CONCERNS ABOUT ECONOMIC SITUATION

17. (SBU) Lee Jooil told Poloff that as the global financial crisis deepens, he is increasingly concerned about the stability of Kazakhstan's economy. Lee stated that, in his personal opinion, "until now, Kazakhstani leaders like Prime Minister Masimov have used oil revenue to placate their people, but Kazakhstan may no longer have the resources to satisfy people's needs." Lee said that some of his contacts think the tenge could be devalued by more than 10 percent, which could severely affect Kazakhstan's foreign debt. Lee also expressed concern that Kazakhstan's economy is not diversified enough, arguing that the problem with oil and uranium is that the prices of such commodities fluctuate so much. He said that while South Korean companies were interested in investing in Kazakhstan's oil and gas sector last year, when oil prices were higher, now that prices are down and capital is tight, extracting oil from the high-cost Caspian Sea environment is just not as attractive anymore. Lee also noted that South Korea, which generates 40 percent of its power from nuclear energy, invested in

Kazakhstan following a sharp spike in the price of uranium in 2008. Lee admitted to Poloff that now that uranium prices are falling again, Korean investors are less enthusiastic about prospective investments in Kazakhstan in this industry.

SOME KOREAN COMPANIES PULLING OUT, CUTTING BACK

18. (SBU) Lee Jooil maintained that the global financial crisis is having its strongest effect on South Korean investments in Kazakhstan's banking and construction sectors. He noted that when Ambassador Kim Il Soo met with Korean companies in Almaty several weeks ago, four of them, including one in banking and another in construction, announced decisions to reduce their work force in Kazakhstan. According to Lee, many small and medium-sized companies in Korea are facing severe capitalization and cash-flow problems; therefore the embassy expects many more Korean businesses to scale back their foreign investments.

19. (SBU) The global financial crisis is particularly affecting the Kazakhstan operations of Highvill, a construction company that is one of Korea's flagship enterprises in the country. The first building developed by Highvill in Kazakhstan is located directly across the river from the Presidential Administration in Astana, and contains a number of luxury features rare in housing complexes in Astana, including an indoor golf driving-range, a fitness center, and sauna and karaoke facilities. Use of these facilities is optional for residents and costs an additional \$210 per month. The U.S. Embassy has two employees with residences in Highvill, and all the South Korean Embassy officials live there, as well as the Ambassador of Switzerland. Highvill sold all of the units in its

ASTANA 00000169 003 OF 003

first block several years ago, and Lee said Highvill representatives told him about wealthy Kazakhstanis bringing suitcases of cash to buy several apartments at once. Since the real-estate crash in Kazakhstan, however, Highvill has had trouble selling its remaining Block 2 units. The exterior of its second tower (containing Blocks 3 and 4) is complete, but Highvill stopped construction on the interior several months ago. On December 21, South Korea's Ministry of Construction awarded Highvill a "B" rating, allowing it to continue its operations under monitoring. (NOTE: The Ministry of Construction issued one Korean construction company which has operations in Almaty a "B" rating, and gave another "C" rating. A "C" rating will result in a government-imposed restructuring of that company. END NOTE.) Despite the temporary reprieve, Lee reported that Highvill executives remain concerned that they may be forced to further scale back, and have applied for Kazakhstani government assistance funds through a program to help the troubled construction industry. However, Lee believes that as a foreign company, Highvill may have difficulty securing such assistance.

HOAGLAND